

IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO

DIVISION OF FINANCIAL MANAGEMENT DECEMBER 2006 VOLUME XXIV NO. 6

Tis the season for lists. Wish lists. Christmas card lists. And, most anticipated, Santa's gift list. Everyone seems busy preparing lists. Economists are no exception. As 2006 wanes, the economists at Global Insight, a national forecasting service, jotted down their thoughts regarding 2007. So, without further delay, and with apologies to David Letterman, we present Global Insight's list of top ten economic predictions for the coming year.

One. The U.S. economy will expand by a sluggish 2.2% in 2007. Consumer spending and capital spending are bearing the weight of the housing downturn. However, spending and investment will be supported by strong fundamentals.

Two. Other economies' will also slow a little. Eurozone GDP increased 2.6% in 2006—its best showing in six years. But its pace will drop to 2.0% in 2007 because of an anticipated increase in interest rates, tighter fiscal policies, the rising euro, and slower export growth. For similar reasons, Japanese economic growth is expected to downshift from 2.7% in 2006 to 1.8% in 2007.

Three. China and India will have healthy economic growth. China's output grew 10.5% in 2006. While Chinese government policies to dampen investment spending make a repeat of last year's stellar showing doubtful, its GDP still is expected to grow 9.5% in 2007. India's economy is predicted to

expand around 8% in 2007. Both China's and India's expected growth rates are well above the 3.2% increase predicted for the entire world.

Four. Oil prices will remain high. The price of oil has been fluctuating around \$60 per barrel for the last four months. It will remain close to this range because of tight oil markets and limited excess capacity. This situation reflects the sluggish real investment in this industry caused by rapidly rising costs. Moreover, OPEC has indicated it will cut production if the price of crude falls below \$60 per barrel.

Five. Core inflation will ease. The very good news is that record-high oil prices have had almost no impact on the core inflation, which means the spillover effect of rising oil prices outside of the energy sector has been minimal. Also, initial estimates of unit labor costs have been revised downwards. It is believed core inflation has already peaked and will fall in 2007.

Six. The Federal Reserve will reduce interest rates three times in 2007, which will take the federal funds rate down to 4.5%. The cuts could begin as early as March, but no later than May. These reductions are made possible due to easing inflationary pressures.

Seven. Housing will dampen U.S. growth. The U.S. housing crunch has already cut GDP growth by more than 1.0% in the second half of

2006. It will remain a drag on growth through much of next year, although its impact will diminish as the year progresses.

Eight. The U.S. current account deficit will shrink slightly. It has been estimated this deficit peaked at more than \$900 billion in the third quarter of 2006. It should average just over \$800 billion in 2007 due to the combination of weaker domestic demand and stronger demand for U.S. exports. Exports are being helped by the dollar's expected slide in 2007 (see number nine).

Nine. The downward pressure on the dollar will not ease. Until recently, the greenback was being pulled in opposite directions. Down by the huge current-account deficit and up by stronger growth and relatively high domestic interest rates. These conditions have changed. Now, the U.S. dollar is under uniform downward pressure thanks to slowing domestic economic growth and the predicted interest rate cuts.

Ten. No recession. Even if the national housing market deteriorates further and housing turns down in other developed countries, the U.S. economy is unlikely to retreat. In fact, no recession is predicted over the foreseeable future.

We would like to add another item to this list: The Division of Financial Management staff wishes everyone a healthy and prosperous New Year!

JAMES E. RISCH, Governor

Division of Financial Management
700 W. Jefferson, Room 122
PO Box 83720

Boise, Idaho 83720-0032 (208) 334-3900

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Brad Foltman, Administrator

Economic Analysis Bureau

Michael H. Ferguson, Chief Economist

Derek E. Santos, Economist

General Fund Update

As of November 30, 2006

<u>Revenue Source</u>	\$ Millions		
	FY07 Executive Estimate ³	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	1,245.3	429.0	442.0
Corporate Income Tax	207.0	55.3	59.4
Sales Tax	1,074.6	421.7	432.9
Product Taxes ¹	21.7	12.6	11.6
Miscellaneous	113.9	28.1	35.4
TOTAL GENERAL FUND²	2,662.5	946.6	981.4

¹ Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
² May not total due to rounding
³ Revised Estimate as of August 2006

General Fund revenue took a break from its spectacular performance in November, coming in \$2.8 million below expectations for the month—the first month in the red so far this fiscal year. Both the individual income tax and the sales tax were slightly below their respective targets for the month, but both also remain solidly ahead of their targets on a fiscal year-to-date basis. Overall the General Fund is \$34.8 million ahead of where it is expected to be (based on the Executive Revenue Forecast) as of the end of November. A new revenue forecast will be released in early January as part of the Executive Budget materials.

Individual income tax revenue was \$2.0 million lower than expected in November, bringing the fiscal year-to-date excess for this category down slightly to \$13.0 million. Withholding collections were the culprit, coming in \$2.9 million lower than expected for the month. This component of the individual income tax is

now \$6.2 million lower than expected on a fiscal year-to-date basis. Filing collections offset about one-third of November's withholding weakness, coming in \$0.9 million higher than expected. The fiscal year-to-date picture is quite similar, except the modest weakness in withholding collections (\$6.2 million short) is swamped by filing collections that are \$18.1 million higher than expected. Together, these two components represent much of the story of what's happening in the individual income tax. Refunds were dead-on in November, a mere \$0.2 million low for the fiscal year to date.

Corporate income tax revenue was almost exactly on target in November, coming in just \$0.1 million above expectations for the month. This revenue category now stands \$4.1 million ahead of the year-to-date predicted value. Estimated payments were \$0.8 million lower than expected for the month, filing payments were \$0.7 million lower than expected, but

this was offset by refunds that were \$1.3 million lower than expected.

Sales tax had its first down month of the fiscal year, coming in \$2.1 million lower than expected in November. Nonetheless, this category is now \$11.2 million ahead of where it was expected to be at this point in the fiscal year. November collections reflect October sales activity, so this is the first month with the new 6% sales tax rate. This implies that some of November's weakness may be due to a "sag" associated with the flip side of accelerated sales in September as consumers rushed purchases to beat the sales tax rate increase.

Product taxes and miscellaneous revenues were both slightly positive, an almost exact repeat of their performance in October. Product taxes were again \$0.3 million higher than expected, and miscellaneous revenue was \$0.9 million ahead of expectations for the month.